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No. 183

In the Supreme Court of the United States

OCTOBER TERM, 1968

A. J. INDUSTRIES, INC., PETITIONER

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF CLAIMS

MEMORANDUM FOR THE UNITED STATES IN OPPOSITION

ERWIN N. GRISWOLD,
Solicitor General,

MITCHELL ROGOVIN,
Assistant Attorney General,

ROBERT N. ANDERSON,
KARL SCHMEIDLER,
Attorneys,
Department of Justice,
Washington, D.C. 20530.

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The question in this case is whether 1958 was the correct year for petitioner to claim an abandonment loss deduction under Section 165(a) of the Internal Revenue Code of 1954 with respect to the underground workings of its Alaska Juneau Gold Mine at Juneau, Alaska.

Petitioner operated the mine from 1897 until 1944. From 1928 until 1942 its operations were highly profitable, and the company declared and paid dividends in excess of $14 million. However, in 1944, after two

successive years of operating losses the mine was shut down. (Pet. App. 6-8, 22.)

Believing that after the war economic conditions would improve, petitioner maintained the mine on a standby condition for eventual reopening. In 1948, in considering whether to use its Juneau assets for other ventures, it was informed that the price of gold would have to be increased to $60 per ounce in order to mine again. After 1948, the economic conditions for gold mining steadily worsened so that by 1958 the gold price would have had to be increased to between $105 and $120 per ounce to justify consideration of reopening the mine. After 1948, petitioner expended substantially less and less funds on maintaining its mine in a standby condition. By 1954 only two of its experienced key men remained in petitioner's employ; its machinery and equipment were becoming worn and obsolete; natural deterioration of the mine increased; and drifts and cave-ins were not corrected because the dwindling personnel could no longer keep up with the increased work. The lower levels of the mine were flooded, not only for preservative measures, but also because the pumping equipment had to be, but was not, replaced. By 1953, it appeared that reopening of the mine was highly unlikely, so petitioner began looking for new businesses. (Pet. App. 22.)

By 1956, petitioner's stockholders were dissatisfied with the policies of the management and elected a new slate of directors who promised "to face up to the fact that there is no prospect of mining gold at a profit from our present properties in the foreseeable future." After Mr. Ver Halen, the leader of the in-

surgent group, had returned from his inspection of the Juneau mine, he realized the mine was inoperable, uneconomic, and unlikely to be operated in the foreseeable future. He recommended that the board immediately begin its acquisition of new businesses. The two mining engineers on the new board expressed their opinion that the mine was noneconomic. The Juneau banks refused to loan even $50,000 on the mining assets. (Pet. App. 23.)

In 1957 the General Appraisal Company told petitioner that the patented lands, mine improvements, mill and ore bodies were of no present economic value. The 1958 report of Wilbur H. Hanson, whom petitioner had hired as an engineer consultant, gave the same opinion. (Pet. App. 14, 23.) In December 1958 petitioner's Board of Directors resolved to abandon the underground workings of the mine as worthless, and the assets were written off as of December 31, 1958.

Petitioner claimed an abandonment loss deduction of over $2,000,000 in its 1958 tax return and a carryback to 1957 and a carryforward to 1959, 1960 and 1961 of the resulting operating loss. The Commissioner of Internal Revenue disallowed the deduction and assessed deficiencies for 1957, 1958 and 1959. Petitioner paid the amounts and brought the present suit for refund. The Court of Claims held that petitioner's Juneau mine became worthless prior to 1958, and dismissed the suit. (Pet. App. 24.)

The decision below is correct. There is no conflict or any other warrant for review by this Court.

1. Section 165(a) of the Internal Revenue Code of 1954 permits the deduction of "any loss sustained during the taxable year and not compensated for by insurance or otherwise." As this Court held in *Boehm* v. *Commissioner*, 326 U.S. 287, 291, in referring to the 1936 precursor of Section 165(a) and the long standing Treasury Regulations on the subject—"deductible losses 'must be evidenced by closed and completed transactions, fixed by identifiable events, bona fide and actually sustained during the taxable period for which allowed.'" See, also, 5 Mertens, *Law of Federal Income Taxation* (Rev.), Sec. 28.04, p. 10.

These general rules apply to losses sustained upon the abandonment of property. As the Court of Claims correctly pointed out (Pet. App. 4-5): "Whether the property actually did lose its useful value in a particular year, and whether the owner actually did abandon it as an asset during that year, are questions of fact to be determined from a consideration of all the surrounding facts and circumstances. * * * The determination as to the year an asset loses its useful value or becomes worthless is a matter of sound business judgment, and that judgment should be given effect unless it appears from the facts that the decision as to the year of loss was unreasonable or unfair at the time the decision was made. Thus, the test is whether the plaintiff has established that under all the facts and circumstances and in the exercise of reasonable business prudence, it fairly determined that its investment in its mine was lost and should be abandoned as worthless in 1958." See, *e.g.*, *Boehm* v. *Commissioner*, *supra*, pp. 292, 293-294; *James*

Petroleum Corp. v. *Commissioner*, 238 F. 2d 678, 680 (C.A. 2); *Mine Hill and Schuylkill Haven R. Co.* v. *Smith*, 184 F. 2d 422 (C.A. 3), certiorari denied, 340 U.S. 932; *Superior Coal Co.* v. *Commissioner*, 145 F. 2d 597, 599 (C.A. 7), certiorari denied, 324 U.S. 864; *Burke* v. *Commissioner*, 283 F. 2d 487, 488-489 (C.A. 9).[1]

Petitioner does not disagree with the court's findings as to what occurred, but contends (Pet. 7-11) that its own subjective belief as to when the mine became worthless should be the controlling or sole criterion in resolving this case. Such a contention was expressly rejected by this Court in *Boehm* v. *Commissioner*, *supra*, pp. 292-293. See, also, *James Petroleum Corp.* v. *Commissioner*, *supra*, p. 680; *Superior Coal Co.* v. *Commissioner*, *supra*; *Mine Hill & Schuyl-*

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[1] The test applied here is identical with the rule of the cases on which petitioner relies, at pp. 7-8 of the petition. Its argument, for which there is no legal precedent, is that the loss deduction may be postponed until the taxpayer, by formal corporate declaration, declares the property abandoned. A taxpayer does not have such discretion to choose the year for which to obtain the tax benefits of the deduction. See *James Petroleum Corp.* v. *Commissioner*, *supra*, p. 680. As the Court of Claims found (Pet. App. 23-24):

> plaintiff's prolonged overstatement of the value of its assets to meet its stock exchange problem, coupled with the obvious tax advantages which accrued, explain eloquently the delay to 1958 in the write-off of the Juneau mine investments. It cannot be ignored that the resolution of plaintiff's board of directors (upon which plaintiff bases its abandonment) was not passed until December 16, 1958, near the end of the first taxable year in which plaintiff made a net operating profit after 14 successive years of net operating loss.

kill Haven R. Co. v. *Smith, supra,* pp. 426-427. It is in all events clear that the insurgents, at the time of their 1956 takeover, had formed the judgment that the property was already valueless.

2. Petitioner's reliance (Pet. 13) upon *Pearl Assurance Co.* v. *United States,* 324 F. 2d 512 (Ct. Cl.), and *Harlan* v. *United States,* 312 F. 2d 402 (Ct. Cl.), is misplaced. In those cases the Commissioner had allowed a loss deduction in the year in which it was claimed, and the court held that the Commissioner should have allowed a carryback of the loss to other years for which refund claims had been filed, but not on grounds of carryback. In the present case, on the other hand, petitioner did not ask the Court of Claims to fix the loss in some other year, if it held that petitioner did not realize the loss in 1958. Even now petitioner only claims that the loss occurred "in either 1956 or 1957," and there is no basis for placing the loss in 1957, the only year prior to 1958 for which a refund was claimed and that was in issue below.

3. The opinion below does not support petitioner's contention (Pet. 12) that it is entitled at least to a deduction for 1956 or 1957 pursuant to the "mitigation" provisions of the 1954 Code. The argument should not be considered because it is made for the first time in this Court. If petitioner meets the complex requirements of Sections 1311(b) and 1312—a matter that was not litigated below and that is by no means as clear as petitioner suggests—the proper course is for it to initiate, for the proper year, the refund procedure required by Section 1314(b) within

one year (*ibid.*) of the day on which the present decision becomes final.

Respectfully submitted.

ERWIN N. GRISWOLD,
Solicitor General,

MITCHELL ROGOVIN,
Assistant Attorney General,

ROBERT N. ANDERSON,
KARL SCHMEIDLER,
Attorneys.

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